LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS

301 State House
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FISCAL IMPACT STATEMENT

LS 7916 **DATE PREPARED:** Feb 3, 2001
BILL NUMBER: HB 1820 **BILL AMENDED:**

SUBJECT: Pension Benefits and Retiree Health Insurance.

FISCAL ANALYST: James Sperlik, Jim Landers
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FUNDS AFFECTED: X **GENERAL**
X **DEDICATED**
FEDERAL

IMPACT: State & Local

Summary of Legislation: (1) The bill permits the surviving spouse of a retired state employee to remain eligible for the retired employee's group health insurance until the surviving spouse remarries or becomes eligible for Medicare. (Current law terminates the surviving spouse's eligibility two years after the date of the retired employee's death.) The bill also permits the surviving spouse of a retired local unit employee to remain eligible for the retired employee's group health insurance until the surviving spouse remarries or becomes eligible for Medicare. (Current law terminates the surviving spouse's eligibility two years after the date of the retired employee's death.)

(2) The bill provides that retirement benefits for members of the Public Employees' Retirement Fund (PERF) and the Indiana State Teachers' Retirement Fund (TRF) are based on the three years of service (rather than five years of service) in which the member's compensation was highest; (3) increases the multiplier used in computing PERF and TRF benefits from 1.1% to 1.5%; (4) provides that for purposes of determining a TRF member's pension benefits, the member's "annual compensation" includes the additional amount that would have been paid to the member under the member's employment contract if the member had not taken unpaid leave of absence during the year to serve in the General Assembly; (5) increases the amount of severance pay included in the determination of final average salary for purposes of computing PERF and TRF benefits from $2,000 to $5,000.

Effective Date: July 1, 2001.

Explanation of State Expenditures: (1) Currently, there are approximately 331 retired state employees participating in the state retiree health insurance program. Of this total, 53 of the retirees purchase family coverage with the balance of 278 purchasing single coverage. Specific data on the number of potential spouses who would be eligible under the new guidelines is not available, although the number is expected to be small. Presumably, most of the eligible surviving spouses would come from the group purchasing family coverage. However, a few individuals from the group purchasing single coverage could be surviving spouses still eligible under the existing two-year limit.

State retirees pay both the employer and employee share of the health insurance premium. In addition, current law requires that a surviving spouse pay the amount that the retired employee would have been required to pay for coverage he or she selects. The annual cost for single coverage ranges from $3,186 per year to $3,859 per year. The State Department of Personnel reports that retirees cost the state more than the actual premium paid due to adverse experience. For every $1 paid by a retiree, the cost to the state is approximately $2.37. Therefore, the additional cost to the state from this provision would be the amount exceeding the premium paid by the surviving spouse after the two-year coverage period already allowed by current law has elapsed. Given the adverse experience factor, the estimated health care cost of each participating surviving spouse would range from $7,551 to $9,146 per year. As a result, the additional cost to the state due to the bill would range from $4,365 to $5,287 for each participating surviving spouse.

The funds affected are the State General Fund and various dedicated funds.

(2) The bill also provides that retirement benefits for members of the Public Employees' Retirement Fund (PERF) and the Indiana State Teachers' Retirement Fund (TRF) are based on the three years of service (rather than five years of service) in which the member's compensation was highest. The impact of this provision is shown in the tables below for PERF and TRF. All estimates below were based on the same data and methods as were used for the most recent annual actuarial valuation as of June 30, 1999.

PERF Final Average Salary Based on 3 Years.

	State	Local Units	Total
Estimated Increase in Unfunded Accrued Liability	$75 M	$91 M	$166 M
Estimated Increase in Annual Funding	$9 M	$12 M	$21 M
Increase in Annual Funding as % of Payroll	0.7%	0.6%	0.7%

The funds affected are the State General Fund (55% or $4.95 M), and various dedicated fund (45% or $4.05 M). The percent split represents the amount each fund contributes to the state budget for personal services.

TRF Final Average Salary Based on 3 Years.

	Closed Plan	Post '96 Plan	Total
Increase in Unfunded Actuarial Accrued Liability	$376 M	$23 M	$399 M
Increase in Contribution Rate as % of Payroll:			
Normal Cost	0.5%	0.5%	0.5%
UAAL (40 yr. amortization)	0.5%	0.2%	0.4%
Total	1.0%	0.7%	0.9%
Increase in Payout			
First Year	$1.5 M.	$20,247	$1.5 M.
Second Year	$3.1 M.	$46,664	$3.1 M.

The fund affected for the Closed Plan is the State General Fund. The Post '96 Plan is actuarially funded by a level percent of payroll by the local school corporations.

(3)The bill also increases the multiplier used in computing PERF and TRF benefits from 1.1% to 1.5%.

PERF

	State	Local	Total
Estimated Increase in Unfunded Accrued Liability	$576 M	$693 M	$1,269 M
Estimated Increase in Annual Funding	$69 M	$91 M	$160 M
Increase in Annual Funding as % of Payroll	5.6%	4.8%	5.1%

The funds affected are the State General Fund (55% or $37.95 M) and various dedicated funds (45% or $31.05 M). The percent split represents the amount each fund contributes to the state budget for personal services.

TRF

	Closed Plan	Post '96 Plan	Total
Increase in Unfunded Actuarial Accrued Liability	$2,150.8 M	$132.8 M	$2,283.6 M
Increase in Contribution Rate as % of Payroll:			
Normal Cost	2.8%	2.8%	2.8%
UAAL (40 yr. amortization)	2.8%	0.8%	2.4%
Total	5.6%	3.6%	5.2%
Increase in Payout			
First Year	$8.8 M	$133,176	$8.9 M
Second Year	$18.4 M	$260,836	$18.6 M

The fund affected for the Closed Plan is the State General Fund. The Post '96 Plan is actuarially funded by a level percent of payroll by the local school corporations.

(4) The bill also provides that for purposes of determining a TRF member's pension benefits, the member's "annual compensation" includes the additional amount that would have been paid to the member under the member's employment contract if the member had not taken unpaid leave of absence during the year to serve in the General Assembly. This section does not affect PERF.

The salary used in the computation would be the member’s base contractual salary as a teacher, rather than the partial amount based on actual teaching service for the year. The specific impact will depend upon the number of TRF members who take unpaid leaves of absence to serve in an appointed or elected position of public service for a period of time toward the end of their teaching career. Assuming the number of members in this category is small relative to the entire TRF active member population, the overall effect on TRF is likely to be small. However, the impact for affected members could be significant. For example, if the final average salary increases to $40,000 from $30,000, the annual TRF benefit for a 30-year teacher would increase to $13,200 from $9,900. The liability associated with the increased benefit for the 30-year teacher who would retire at age 60, for example, would be over $30,000. The fund affected is the State General Fund for the Closed Plan.

(5) This bill also increases the amount of severance pay included in the determination of final average salary for purposes of computing PERF and TRF benefits from $2,000 to $5,000.

<u>PERF</u>

	State	Local	Total
Estimated Increase in Unfunded Accrued Liability	$317,000	$381,000	$698,000
Estimated Increase in Annual Funding	$38,000	$50,000	$88,000
Increase in Annual Funding as % of Payroll	Trace	Trace	Trace

The funds affected are the State General Fund (55% or $20,900) and various dedicated funds (45% or $17,100). The percent split represents the amount each fund contributes to the state budget for personal services.

<u>TRF</u>

	Closed Plan	Post '96 Plan	Total
Increase in Unfunded Actuarial Accrued Liability	$168 M	$10 M	$178 M
Increase in Contribution Rate as % of Payroll:			
Normal Cost			
UAAL (40 yr. amortization)	0.2%	0.2%	0.2%
	<u>0.2%</u>	<u>0.1%</u>	<u>0.2%</u>
Total	0.4%	0.3%	0.4%
Increase in Payout			
First Year	$0.7 M	$9,154	$0.7 M
Second Year	$1.4 M	$21,097	$1.4 M

The fund affected for the Closed Plan is the State General Fund. The Post '96 Plan is actuarially funded by a level percent of payroll by the local school corporations.

<u>Explanation of State Revenues:</u>

<u>Explanation of Local Expenditures:</u> (1) Data is not available regarding the number of singles and families participating in retiree health insurance programs at the local level or on the number of surviving spouses of local unit employees who would be eligible for this benefit. However, the number is expected to be small.

Cost data for local unit employees also is not readily available. It is assumed that local retirees mirror state retirees and that the adverse experience listed for retired state employees would apply in this case, too.

The impact for items 2 through 5 can be found in the tables in Explanation of State Expenditures.

Explanation of Local Revenues:

State Agencies Affected: All

Local Agencies Affected: Local Government Units and School Corporations.

Information Sources: Keith Beesley, State Department of Personnel, 232-3062; Doug Todd of McCready & Keene, actuaries for PERF, 576-1508; Denise Jones of Gabriel Roeder Smith & Co., actuaries for TRF, 1-800-521-0498.

DEFINITIONS

Amortization Paying of an interest-bearing liability by gradual reduction through a series of installments as opposed to paying it off by one lump sum payment.

Final Average Salary--Final average salary is that measure of a participant's level of earnings which is based on his average rate of salary for a specified period of time, usually the three, five, or ten years immediately preceding retirement. A participant's final average salary may be one of the factors used in determining the amount of his benefits.

Funding- a systematic program under which assets are set aside in amounts and at times approximately coincident with the accruing of benefit rights under a retirement system.

Normal Cost- current value of benefits likely to be paid on account of members' service being rendered in the current year.

Unfunded Actuarial Liability (sometimes called the unfunded liability) of a retirement system at any time is the excess of its actuarial liability at that time over the value of its cash and investments.